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Executive Board of the United Nations Entity for Gender Equality and the Empowerment of Women

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Progress report towards a harmonized cost-recovery policy

Summary

The present report gives an overview of the current status of the progress made by both the United Nations Entity for Gender Equality and the Empowerment of Women and other United Nations funds and programmes towards achieving a harmonized cost-recovery policy.

It summarizes the findings of the United Nations Development Programme, the United Nations Children's Fund and the United Nations Population Fund, as presented in their joint paper (DP-FPA/2012/1-E/ICEF/2012/AB/L.6) and presents conclusions on the ongoing approach to be taken.

The Executive Board may wish to review and take note of the conclusions drawn and endorse the formal involvement of the Entity in the inter-agency working group.

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I. Background

1. The Executive Board of the United Nations Entity for Gender Equality and the Empowerment of Women (UN-Women), in paragraph 12 of its decision 2011/5 on the biennial institutional budget for the Entity for 2012-2013 (see UNW/2011/13), requests the Under-Secretary-General/Executive Director to submit, for the consideration of the Executive Board at its second regular session of 2012, proposals for the principles, criteria and procedures that should guide the use of cost-recovery income, taking into account the harmonized cost-recovery policies and methodologies used by the United Nations Children's Fund, the United Nations Development Programme and the United Nations Population Fund.

2. The United Nations Children's Fund (UNICEF), the United Nations Development Programme (UNDP) and the United Nations Population Fund (UNFPA) undertook a joint review during 2012 of their current cost-recovery principles, policies and approaches. The review recommended a number of fundamental changes to the current methods for calculating and recovering such costs. The entities have prepared a joint report to their respective Executive Boards (see document DP-FPA/2012/1-E/ICEF/2012/AB/L.6). The paper was considered at the second regular session of 2012 of each of their Executive Boards. Major changes have been discussed informally with representatives of the Executive Boards; however, a number of significant issues remain subject to further analysis by the entities. The organizations plan to complete these analyses and hope to obtain final approval for the new approach early in 2013, with implementation commencing in the integrated budgets for 2014-2015.

3. During this time, UN-Women has worked closely with the entities to understand how the proposed changes might affect its existing cost-recovery policy and methodology. Given the major changes expected to occur in cost-recovery methodology, UN-Women cannot at this time present the final set of proposals requested by the Executive Board in its decision 2011/5 if it is to ensure harmonization with the approaches of the three entities, as was also requested.

4. The present document therefore builds on the analysis and conclusions of the joint review paper and contains (a) a brief overview of the current approach of UN-Women in relation to cost recovery; (b) a review of UN-Women alignment with the harmonization process; (c) a summary of the major conclusions and recommendations of the joint review carried out by the three entities and their implications for UN-Women; and (d) the next steps to be taken by UN-Women in developing proposals for the principles, criteria and procedures, in collaboration with the organizations, for cost recovery. The document concludes with a set of proposals for areas in which the Board may wish to give guidance to the Entity.

II. Overview of the current approach of the Entity in relation to cost recovery

5. The cost-recovery approach that UN-Women currently follows has been carried over from the United Nations Development Fund for Women (UNIFEM), which followed an approach based on a harmonized set of principles and cost definitions commonly accepted by United Nations system organizations, as follows:

Harmonized cost-recovery principles

(a) In a multi-funded organization (receiving both regular and other resources), each source of funding should bear all attributable costs relating to the necessary management provided by the organization;

(b) All costs can be classified as direct, fixed indirect or variable indirect costs, based on the mandate and business model of each organization;

(c) While United Nations organizations have agreed on a common definition of cost categories, each organization must match its costs against the categories to make them meaningful. Cost recovery would generally apply to variable indirect costs.

Cost classification: harmonized cost definitions

(a) **Direct costs.** Direct costs are all costs that are incurred for, and can be traced in full to, the activities, projects and programmes of an organization in fulfilment of its mandate. Included are the costs of project personnel, equipment, project premises, travel and any other inputs necessary to achieve the results and objectives established for programmes and projects;

(b) **Fixed indirect costs.** These are all costs incurred by the organization, regardless of the scope and levels of its activities, that cannot be traced unequivocally to specific activities, projects or programmes. These costs typically include the top management of an organization, its corporate costs and statutory bodies not related to service provision.

(c) **Variable indirect costs.** Variable indirect costs are all costs incurred by the organization as a function and in support of its activities, projects and programmes that cannot be traced unequivocally to specific activities, projects or programmes. These costs typically include services and administrative units, as well as their related system and operating costs.

6. In UNIFEM, cost recovery applied to both the variable indirect and direct cost components. With regard to the variable indirect cost, UNIFEM adopted the harmonized cost-recovery methodology and rate of 7 per cent agreed upon by the entities, based on a harmonized calculation methodology as described in annex I. However, the rates calculated by the individual organizations differed, as was expected given their differing sizes and business models. The decision to apply the harmonized rate of 7 per cent was taken to support the notion of harmonization among UNDP, UNFPA and UNICEF and to avoid fostering competition among them based on recovery rates. As a result, the existing policy followed by UN-Women is a single rate of 7 per cent to recover the variable indirect costs of managing projects and/or programmes funded from non-core resources (earmarked funds).

III. Participation of the Entity in the inter-agency harmonization process

7. In response to decision 2011/5 of the Executive Board, UN-Women has joined the entities to participate in the adoption of an integrated budget, starting in 2014. As a result and in accordance with the same decision, the biennial institutional budget for 2012-2013 was prepared and approved on the basis of the harmonized

cost classification and results methodologies approved for UNDP, UNFPA and UNICEF. The cost categories are: development activities, subdivided into programme and development effectiveness; United Nations development coordination activities; management; and special purpose (please refer to annex II for further information). The cost categories are defined as follows:

(a) **Development activities.** The corresponding costs are associated with programmes and development effectiveness activities that contribute to and are essential for the realization of effective development results, as follows:

(i) **Programmes.** Activities and associated costs traced to specific programme components or projects, which contribute to delivery of development results contained in country, regional or global programme documents or other programming arrangements;

(ii) **Development effectiveness.** The costs of activities of a policy and/or advisory nature, and of technical and implementation nature that are needed to achieve the objectives of programmes and projects in the focus areas of the organizations. These inputs are essential to the delivery of development results, and are not included in specific programme components or projects in country, regional or global programme documents;

(b) **Management.** This comprises activities and associated costs whose primary function is the promotion of the identity, direction and well-being of an organization. These activities include executive direction, representation, external relations and partnerships, corporate communications, legal, oversight, audit, corporate evaluation, information technology, finance, administration, security and human resources;

(c) **United Nations development coordination.** This comprises activities and associated costs supporting the coordination of development activities of the United Nations system;

(d) **Special purpose.** This covers activities and associated costs of (i) capital investments; and (ii) services to other United Nations organizations.

8. Over the past few months, UN-Women has reviewed the detailed cost-recovery policies and procedures used by UNIFEM, including the allocation of recovered funds, in the context of current requirements and the evolving new harmonized approach being proposed by UNICEF, UNDP and UNFPA to their Executive Boards. The work done to date will facilitate the preparation of cost-recovery policies and procedures tailored to the organization's business practices and harmonized with the new approach of the other entities.

IV. Major conclusions and recommendations of the joint cost-recovery review

9. The joint review, which was sponsored by the three entities and carried out by a consulting firm, examined the organizations' business models, benchmarked a number of international organizations and developed proposals for a harmonized framework for defining and attributing organizational costs and a cost-recovery calculation methodology. The conclusions reached and agreed to by the entities were based on and aligned with the harmonized cost classifications previously

approved by their respective Executive Boards and utilized in the institutional budgets for 2012-2013 and were intended to increase simplicity, transparency and comparability.

10. A proposed harmonized conceptual framework has been developed to define and attribute organizational costs in the context of the integrated budget, from 2014 onwards. Details of the proposed harmonized conceptual framework for defining and attributing organizational costs, as excerpted from document DP-FPA/2012/1-E/ICEF/2012/AB/L.6, can be found in annex II.

11. The two most significant changes proposed are (a) that the distinction between fixed and variable indirect costs no longer be used in calculating cost recovery, with the result that all indirect costs be considered in calculating cost recovery and (b) that development effectiveness activities and associated costs be directly funded from core and non-core resources. Therefore, recovered costs would cover a proportional share of management and comparable special purpose costs.

12. The entities also recommend to their Executive Boards that the proposed harmonized cost-recovery rate calculation should factor in an assured level of core resources that would be available to each organization to ensure the funding of those critical, cross-cutting functions and activities that underpin the integrity of their business models and mandates, though there is currently no clear definition of what would be included. Because of the differing business models of the three entities, they further recommend that the funding of development coordination activities and associated costs be addressed in the context of each organization's integrated budget proposals rather than as part of the harmonized framework.

V. Preliminary analysis of the implications of the proposed harmonized conceptual framework on the cost-recovery methodology of the Entity

13. UN-Women has extensively consulted with the entities and, in addition, has participated in the joint informal sessions of the Executive Boards of UNDP/UNFPA, that were organized to discuss the harmonized cost-recovery methodology in the context of the integrated budget, starting in 2014. The recommendations emanating from the joint review did not lead to the endorsement by the organizations of either a clear cost-recovery methodology or rate. In paragraph 28 of the joint review by UNDP, UNFPA and UNICEF, it is indicated that further analysis and consultations are required to determine whether (a) the current harmonized methodology, from which the existing harmonized rate of 7 per cent is derived, remains appropriate; (b) core donors currently bear an undue share of organizational costs; and (c) the cost-recovery rate for each organization lends itself to harmonization.

14. In conclusion, and based on the findings of the joint review, the entities are seeking further guidance from their respective Executive Boards on the determination of the final cost-recovery rates to be adopted for the period from 2014 to 2017.

15. The potential implications for UN-Women could be significant and result in changes to the current cost-recovery rate. It should be noted, in addition, that a portion of development effectiveness activities, previously funded from the

institutional budget, would need to be directly funded from projects and programmes. This represents $40 million, or 28.3 per cent of the institutional budget for 2012-2013. With regard to the current cost-recovery rate, the Executive Board approved a gross budget while permitting the organization to utilize any cost-recovery resources above the estimated amount to support the institutional budget, on the understanding that a prudent approach was required for the biennium 2012-2013.

16. In addition, it should be noted that the funding for UN-Women is, at present, almost equally split between regular and other resources, although it is clear that this ratio may change as the organization matures.

17. Furthermore, unlike the other entities, UN-Women is also funded from assessed contributions through the regular budget, which represents an approximate annual amount of $7.2 million, and there is a need to determine whether the functions covered under the regular budget should be considered as an integral part of the cost-recovery methodology.

VI. Next steps for the Entity in moving towards a harmonized cost-recovery approach

18. At this juncture, UN-Women is not in a position to put forward a proposal of a harmonized cost-recovery methodology or rate, as had been requested by the Executive Board in its decision 2011/5, in view of the current status of the harmonized cost-recovery approach involving UNDP, UNFPA and UNICEF.

19. In parallel with the other entities involved in developing a harmonized cost-recovery approach, UN-Women will continue to use the current cost-recovery rate and utilization methods for the remainder of the current biennium, with the goal of adopting the new approach for the integrated budget for 2014-2015, subject to approval by the Executive Board.

20. In the short term, UN-Women will continue to work with the entities as they receive additional guidance from their Executive Boards and carry out the analyses necessary to provide the details required to gain approval of the new approach and to permit its implementation in the coming biennium. UN-Women will inform the Board of any major changes to the proposal that are made as a result of the actions of the Executive Boards of the organizations.

21. Given the current expectations of progress by the entities in completing their analyses and support from their Executive Boards, UN-Women intends to present to the Executive Board, at its first regular session of 2013, a proposed set of principles, criteria and procedures to guide the collection and use of cost-recovery income, as harmonized with the approach taken by the three organizations.

VII. Conclusions

22. Based on the discussion above, UN-Women proposes that the Executive Board:

(a) Note that the current cost-recovery approach and methodology used by UN-Women is harmonized with that of UNICEF, UNDP and UNFPA;

(b) Affirm its request that the Under-Secretary-General/Executive Director ensure that all sources of funding bear their fair share of management costs and avoid the subsidization of non-core voluntary resources by core voluntary resources;

(c) Request UN-Women to formally join the inter-agency working group with the objective of arriving at a harmonized cost-recovery framework and methodology;

(d) Request the Under-Secretary-General/Executive Director to submit to the Board, at its first regular session of 2013, proposals for the principles, criteria and procedures that should guide the management of cost-recovery income, in a joint paper produced in conjunction with the entities;

(e) Request that the proposals be accompanied if necessary by a description of the transitional arrangements needed to assure incorporation of the new harmonized approach in the proposals for the integrated budget for 2014-2015.

Annex I

Harmonized calculation for the cost-recovery rate

The analytical approach to developing the existing harmonized cost-recovery rate was calculated as follows:

1. Total the amounts required for the institutional budget.

2. Subtract from this the aggregate fixed indirect costs.

3. The amount in 2. equals the variable indirect costs to be recovered.

4. Take the amount calculated in 3. and split it proportionally, according to the levels of planned core and non-core resources.

5. Take the amount calculated in 4. to be recovered by non-core resources and calculate it as a percentage of planned non-core programme resources.

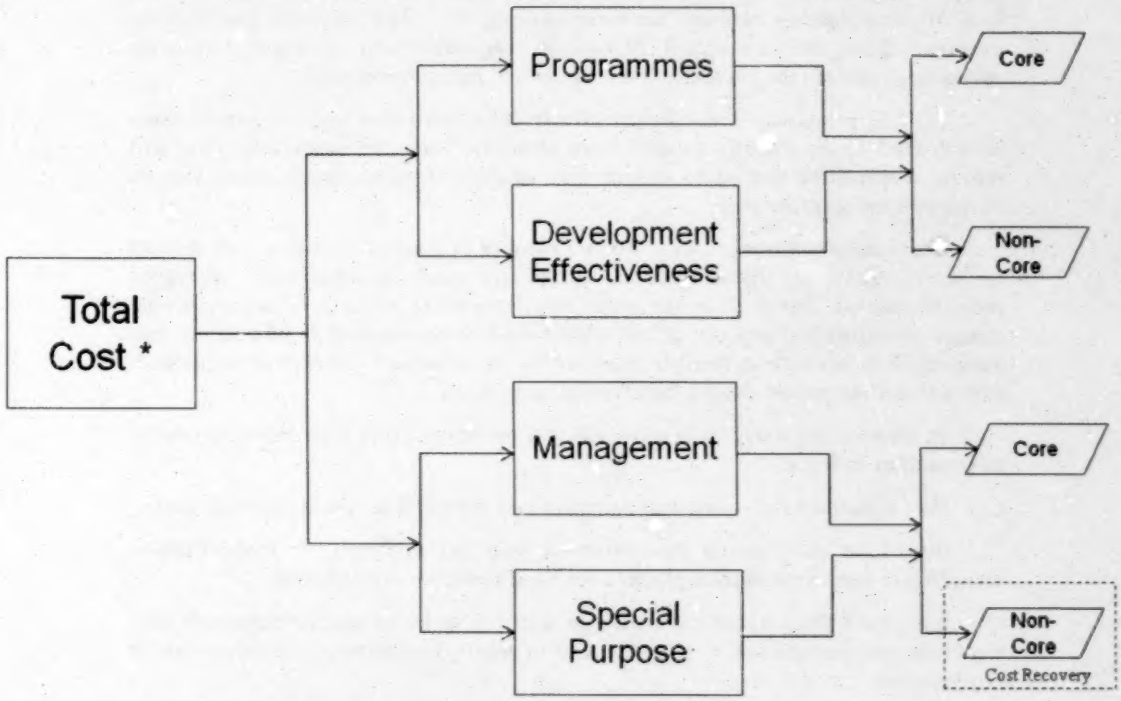
6. The amount in 5. equals the required non-core cost-recovery rate.

Annex II

Details of the proposed harmonized conceptual framework for defining and attributing organizational costs

The following is an extract from document DP-FPA/2012/1-E/ICEF/2012/AB/L.6 (fig. 1 and paras. 20 to 24).

Proposed harmonized conceptual framework for defining and attributing organizational costs



Note: * Excludes activities and associated costs of a non-comparable nature, such as those relating to United Nations development coordination activities and special-purpose activities (United Nations Volunteers (UNV) and the United Nations Capital Development Fund).

The proposed harmonized conceptual framework outlined above has the following implications:

(a) In principle, all management activities of the three entities, and such comparable special-purpose activities as capital budgets, would be funded with a level of proportionality through cost recovery. The funding of the activities would be with a level of proportionality shared between core and non-core resources;

(b) Given the unique, ongoing nature of United Nations development coordination activities, and special-purpose activities (United Nations Volunteers (UNV) and the United Nations Capital Development Fund), there continues to be a lack of comparability between the three entities. It is thus proposed that they be excluded from the conceptual framework and addressed separately by each organization within the context of their integrated budget proposals;

(c) In principle, development effectiveness activities and associated costs would need to be directly funded from core and non-core resources. This will require a transition period to ensure that adequate funding mechanisms can be developed and implemented.

The conceptual framework reflects a number of positive elements with respect to cost recovery (harmonization, simplicity and transparency, increased proportionately). But it also has major implications in relation to organizational change and financial aspects, all of which need to be thoroughly considered and planned for in advance. A flexible implementation of the new conceptual framework over a transition period should therefore be considered.

In view of the above, it is proposed that the harmonized cost-recovery rate be calculated as follows:

(a) Calculate the sum of management and comparable special-purpose costs;

(b) Take the amount calculated in step (a) and split it proportionally according to the levels of total planned core and non-core expenditures;

(c) Take the amount calculated in step (b) to be recovered from non-core resources and calculate it as a percentage of total planned non-core development expenditures;

(d) The amount in step (c) equals the notional cost-recovery rate on non-core resources.

The proposed harmonized cost-recovery-rate calculation should also factor in an assured level of core resources that would be available to each organization to ensure the funding of those critical, cross-cutting functions and activities that underpin the integrity of their business models and mandates.

The harmonized conceptual framework and cost-recovery calculation methodology will have an important impact on the extent to which cost-recovery rates can be harmonized and a harmonized proportional attribution of organizational costs between core and non-core resources can be achieved.

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Proposed approach for calculating the operational reserve for the United Nations Entity for Gender Equality and the Empowerment of Women

Summary

The present report outlines a proposed approach for calculation of an operational reserve in compliance with financial regulation 19.2(a) of the financial regulations and rules of the United Nations Entity for Gender Equality and the Empowerment of Women (UN-Women). The proposed approach is submitted for the consideration of the UN-Women Executive Board.

The Executive Board may wish to review and approve the proposed methodology for calculation of the operational reserve and the establishment of a reserve for field office accommodation.

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I. Introduction

1. Financial regulation 19.2 of the financial regulations and rules of the United Nations Entity for Gender Equality and the Empowerment of Women (UN-Women) states:

> Within the account held by UN-Women, the following reserves shall be established at levels set by the Executive Board:
>
> (a) An operational reserve, the purpose of which is to guarantee the financial viability and integrity of UN-Women. The reserve shall be fully funded and held in irrevocable and promptly available liquid assets. The elements to be compensated for and covered by it shall be limited to:
>
> (i) Downward fluctuations or shortfalls in resources;
>
> (ii) Uneven cash flows;
>
> (iii) Increases in actual costs as compared to planning estimates or fluctuations in delivery; and
>
> (iv) Other contingencies that result in a loss of resources for which UN-Women has made commitments for programming.
>
> The decision to make a drawdown from the operational reserve shall rest solely with the Under-Secretary-General/Executive Director, who will report all drawdowns to the Executive Board at its next regular session and, in between sessions, to members of the Executive Board as may be prescribed by the Board or whenever the situation in the Under-Secretary-General/Executive Director's opinion so merits;
>
> (b) A fully funded reserve for field office accommodation for housing for internationally recruited, field personnel financed by UN-Women and for office accommodation; and
>
> (c) Such other reserves as may be approved by the Executive Board.

2. With regard to subparagraph (b) of the regulation, it is the responsibility of international staff to provide their own personal accommodation. At the end of 2011, estimated commitments relating to field offices remained relatively low ($1 million for 2011). A separate reserve for field accommodation is proposed under section VII below.

3. Other resources are normally credited to the other resources account in advance of UN-Women entering into commitments, in compliance with regulation 3.7(b) of the UN-Women financial regulations and rules, which states that "Contributions [to other resources] shall be paid in advance of the allocation made for the implementation of planned programme activities of UN-Women …". Hence only regular resources (excluding assessed contributions) have been taken into account in reviewing the need for an operational reserve because there is limited risk of a cash shortfall of other resources.

II. Existing UN-Women operational reserve

4. On 1 January 2011, when UN-Women became operational, $21 million was transferred from the former United Nations Development Fund for Women (UNIFEM) that had been set aside by UNIFEM as an operational reserve. The approach taken by UNIFEM for calculating the operational reserve was to set a three-year ceiling on approved programme budgets from regular resources, then calculate the operational reserve as one third of the three-year ceiling, adjusted for anticipated delivery rates.

5. UN-Women merges and builds on the important work of four previously distinct parts of the United Nations system that focused exclusively on gender equality and the empowerment of women:

(a) Division for the Advancement of Women;

(b) International Research and Training Institute for the Advancement of Women (INSTRAW);

(c) Office of the Special Adviser on Gender Issues and Advancement of Women ;

(d) UNIFEM.

6. UN-Women is therefore fundamentally different, from an operational perspective, from UNIFEM. For instance, it has a larger and more diverse donor base, an expanded management and operational infrastructure, an expanded and different field office presence with designated UN-Women representatives and new organizational procedures and programme planning arrangements.

7. It is therefore necessary to redefine the approach to the operational reserve. A key objective in this regard is to maximize the resources available for programming, while ensuring the retention of an optimal operational reserve level that takes fully into account the risk profile of UN-Women and the impact of budgetary planning and liquidity management approaches already in place. As UN-Women became operational only on 1 January 2011, limited relevant financial information is available for historical analysis.

III. Approaches by selected other United Nations organizations

8. As part of the analysis and to support the decision making process, UN-Women has also reviewed the methodologies adopted by other United Nations organizations to ensure that it builds on the experience of others in its assessment of the risks to be included and that a full understanding of the potential options has been achieved. These United Nations organizations have been chosen as they represent a cross section of entities that either have a relatively similar funding structure to UN-Women or are part of the joint budget harmonization process. A detailed overview of the current policies adopted by the respective organizations is presented in the annex to the present document. A summary of the positions taken is shown below:

Organizations	*Operational reserve*	*Liquidity*
United Nations Children's Fund	N/A	10% of following year's regular resources income
United Nations Population Fund	20% net of regular resources income and a reserve for field accommodation	
United Nations Development Programme	Complex risk based formula	
Office of the United Nations High Commissioner for Refugees	Greater of 10% of annual budgeted programme activities or $10m	Fixed $50 million

IV. Key considerations and existing risk mitigators

9. In reviewing and assessing the preferred approach, the existing procedures in place to minimize the exposure of UN-Women to liquidity risk have been identified to facilitate a decision on the level of operational protection that is needed going forward. The processes already in place within the organization to ensure close control over its cash position and ability to maintain operational functions are:

(a) Short-term imbalances between income and expenditure are primarily managed through the use of working capital (the pool of financial resources that an organization holds which can be used to meet its short-term obligations);

(b) With regard to regular resources (excluding assessed contributions), predictability and reliability are key to establishing the balance between income and expenditure planning. UN-Women is strongly encouraging multi-year pledges and expansion of the donor base. In 2011, 117 Governments contributed to core funds, up from 106 Government donors in 2010. Out of the core contributions from these 117 Governments, 30 were submitted as a multi-year pledge, whereas at the inception of UN-Women in 2010 very few pledges by donors from the Development Assistance Committee of the Organization for Economic Cooperation and Development were in the multi-year format. UN-Women has now obtained multi-year pledges from six major donors amounting to an significant portion (about 60 per cent in an amount of approximately $72 million) of its total regular resources base. This is a development that will enhance the predictability of regular funding for UN-Women;

(c) At the end of 2011, the accumulated surplus (unexpended resources) of UN-Women amounted to approximately $41 million available under regular resources (excluding assessed contributions). In addition, the existing operational reserve of $21 million brought forward from UNIFEM will be maintained unless its use is required. These two elements provide significant security in respect of the potential implications of shortfalls or delay in receipt of funding.

V. UN-Women financial management framework

10. UN-Women maintains close control over planning and allocation processes for its regular resources as well as over ensuring that its liquidity management is tightly controlled. To achieve this, and to minimize the existing risk in relation to cash shortfalls, the following measures are in place:

(a) **Institutional budget**. The institutional budget, which as the operational base of UN-Women has first call over the regular resources and totals $132.3 million net ($ 140.2 million gross) for the period 2012-2013, has appropriations that are approved by the Executive Board on a biennial basis, but are allocated to units on an annual basis. During the first year of the budget period, UN-Women therefore has flexibility to adjust the allocations for the second year. This ensures that the adverse impact of any likely decrease in funding can be reduced through close review of the variable elements of operating costs, in particular, and close management of staffing policies and hiring if required;

(b) **Regular resources and programme allocations**. UN-Women issues only annual core programme allocations, not multi-year allocations, allowing the level of resources allocated to each unit to be changed as circumstances evolve. The annual allocations are based on annual workplans, each of which undergoes a detailed review at headquarters before it can be approved and resources allocated. As a further risk management tool, a minimum of 10 per cent of the projected revenue receipts is held back at the beginning of the year, allowing adjustments in the fourth quarter if necessary;

(c) **Cash flow forecasting**. A cash flow forecast is prepared on a monthly basis for management reporting purposes, taking into account cash inflows, all known commitments and expected cash outflows. This analysis gives a clear indication of the anticipated level of receipts and expenditure and the projected cash balances available for the end of the year. Review of this cash flow forecast ensures that timely action can be taken should there be a shortfall in regular resources funding;

(d) **Liquidity management**. At the end of 2010, UN-Women carried forward $15 million of accumulated surplus (unexpended resources) within its regular resources. At the end of 2011, this had increased to $41 million, which is sufficient to cover approximately 4 months of estimated annual expenses. This, coupled with close review of cash inflows, further ensures that quick and decisive action can be taken if potential liquidity problems become apparent. The accumulated surplus is an integral part of the financial statements that carries forward the balance of unspent resources. This is in line with the organization's business model, which operates on a multi-year commitment basis, resulting in amounts being budgeted but not necessarily spent in any given period.

11. UN-Women uses Atlas to manage its operations. Atlas is an integrated enterprise resource planning system, which is also used by UNDP and other organizations of the United Nations system. The Atlas system facilitates the continuous monitoring of resource utilization, and therefore enables proactive management of liquidity levels to address evolving circumstances. Within Atlas, automated controls limit the risk of spending above approved allocations. These controls ensure that field offices cannot spend more than their original budget allocation and, if needed, this allocation could be reduced. At headquarters, the oversight of expenditures means that action can be taken if any areas are likely to exceed the budget.

12. Based on the existing financial management framework detailed above and the ongoing continual review of the operating capacity of UN-Women, a four month coverage of estimated annual expenses is therefore believed to be a suitable and sufficient level of available cash resources.

VI. Operational reserve proposal

13. Taking into account the existing liquidity management structure, the financial management framework, the approach taken by other organizations and the existing operational reserve inherited from UNIFEM, UN-Women suggests application of a methodology that provides a level of security within the cash balance and minimizes the risk of cash shortfalls as much as possible. To achieve this, UN-Women proposes:

(a) Continuing to follow its current tight controls over liquidity management and holding approximately 4 months of estimated annual expenditure in hand;

(b) Sourcing 50 per cent of this balance through its existing accumulated surplus (unexpended resources) and holding the remaining 50 per cent within its operational reserve, subject to subparagraph (c) below;

(c) Ensuring that the operational reserve maintains a minimum balance equal to the $21 million brought forward from UNIFEM.

14. Based on the above proposal, the potential levels of the operational reserve for the period 2012-2013 would be as follows:

(Millions of United States dollars)

Year	*Regular resources income*	*Estimated annual expenditure*	*Four months of estimated annual expenditure*	*Funding from accumulated surplus (50%)*	*Operational reserve (greater of 50% or $21 million)*
2012	150.0	120.0	40.0	20.0	21.0
2013	200.0	160.0	53.3	26.7	26.7

15. This proposal achieves a balanced approach between both ongoing liquidity and cash flow management, coupled with the maintenance and development of the existing operational reserve. It combines the approach taken by other organizations and ensures that the risk to UN-Women of a cash shortfall is minimized.

VII. Reserve for field office accommodation

16. In accordance with financial regulation 19.2, it is proposed to establish a reserve for field office accommodation. With the establishment of regional offices and the ongoing potential for increased participation in United Nations common premises, UN-Women may incur additional costs to finance its share, if needed, of related construction costs.

17. A reserve of $1 million is proposed, against which UN-Women can make drawdowns, and which will be replenished from the accumulated surplus on an annual basis.

Annex

Methodologies used by organizations that are similar to UN-Women

United Nations Children's Fund

1. The United Nations Children's Fund (UNICEF) does not have an operational reserve, justified by the fact that it employs financial management techniques and processes to plan spending requirements against reasonable income expectations, while maximizing resources available to programmes. The primary financial management techniques and processes are:

(a) A medium-term financial plan, updated annually. This is a rolling four-year income and expenditure plan, which determines the affordable levels of regular resources for programmes;

(b) A multi-year funding framework. The annual pledging event is one element of the multi-year funding framework, at which donors are expected to make funding level commitments and provide payment schedules for the next year, and commitments or indications for the following three years. This predictability provides for assured programme planning and improved cash flow management;

(c) Country programme recommendations, which present for each country the results to be achieved and the financial resources required. The financial projections in the country programme recommendations are estimates based on the best information available at the time because they are forecasted for up to five years into the future, with limited assurance at the time of estimation of actual income;

(d) Every two years, an approved institutional (formerly biennial support) budget, which incorporates the relevant two-year projected regular resources budget for the programme, programme support, and management and administration of the organization;

(e) Integrated project and financial systems that enable UNICEF to continually monitor resource utilization and spot accumulating underemployed resources in the field, and therefore to manage cash levels to meet evolving circumstances.

2. To ensure adequate liquidity, UNICEF maintains year-end cash balances of regular resources income at approximately 10 per cent of the expected regular resources income for the following year.

United Nations Population Fund

3. The operational reserve held by the United Nations Population Fund (UNFPA) was established for the purpose of guaranteeing the financial viability and integrity of the organization. The reserve is fully funded and held in irrevocable and promptly available liquid assets. The level of the operational reserve, established at the end of each year, is calculated at 20 per cent of the net contribution revenue of regular resources for that year. The elements to be compensated for and covered by it are limited to:

(a) Downward fluctuations or a shortfall in resources;

(b) Uneven cash flows;

(c) Increases in actual costs as compared with planning estimates or fluctuations in delivery;

(d) Other contingencies that result in a loss of resources for which UNFPA has made commitments for programming.

4. The decision to make a drawdown from the operational reserve rests solely with the Executive Director, who is required to report all drawdowns to the Executive Board at its next regular session and in between sessions.

5. The reserve has been increased gradually, with annual status updates presented to the Governing Council, including additions and drawdowns.

United Nations Development Programme

6. The operational reserve of the United Nations Development Programme (UNDP), set in 1970, was initially a fixed (and unfunded) amount of $150 million. Because the reserve was not funded, cash was not set aside and was therefore available for spending on programmes. Only after a liquidity crisis in 1975 did UNDP start to fully fund its operational reserve, starting with $15 million in 1977. UNDP was given four years, up to 1980, to fund fully the $150 million.

7. In 1980 a percentage basis was adopted at 25 per cent of estimated contributions or expenditure, whichever was higher. This was reduced to 20 per cent in 1990 on the basis that better information systems and procedures allowed a faster response to adverse financial risks.

8. The current approach of UNDP to the operational reserve was defined in a paper presented to its Executive Board in 1999 (DP/1999/5/Rev.l), based on a financial risk assessment. The formula is relatively complex, with separate elements for income, expenditure, liabilities and structural and cash flow related risks.

Office of the United Nations High Commissioner for Refugees

9. The operational reserve of the Office of the United Nations High Commissioner for Refugees (UNHCR) is established in its financial rules at the higher of $10 million or 10 per cent of budgeted annual programmed activities in the annual programme budget (pillars 1 and 2 of the programme). For the budget year 2012, the approved level is $248.8 million. The operational reserve is primarily for funding unexpected, urgent expenses not already programmed for and is therefore not for the same purposes as the reserve of UN-Women.

10. More comparable is the UNHCR Working Capital and Guarantee Fund, which may be utilized to replenish the operational reserve and generally provides funding pending receipt of contributions pledged within limits set in the financial rules,[a] and to replenish the operational reserve. The Working Capital and Guarantee Fund is a fixed amount, currently set at $50 million.

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[a] Up to one twelfth (8.3 per cent) of the annual budget (all pillars) during the year but not be more than 3 per cent of the annual budget at the end of the year.

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Executive Board of the United Nations Entity for Gender Equality and the Empowerment of Women

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Evaluation and audit matters

Report on internal audit and investigation activities for the period 1 July 2010 to 31 December 2011

Summary

The present report provides information on the internal audit and investigation function of the United Nations Entity for Gender Equality and the Empowerment of Women (UN-Women) for the period from 1 July 2010 to 31 December 2011.

The internal audit and investigation function for UN-Women is performed by the UN-Women Audit Unit of the Office of Audit and Investigations of the United Nations Development Programme (UNDP) on the basis of the Financial Regulations and Rules of UN-Women and a service level agreement on the provision of internal audit and investigation services. During the transitional period in question, those services were provided on the basis of the 2008 service level agreement with the predecessor entity, United Nations Development Fund for Women (UNIFEM), and an interim agreement between UN-Women and the Office of Audit and Investigations signed in early 2011.

The report describes the internal audit function and its activities as well as the main audit results that provide insight into the utilization and management of UN-Women resources.

The Executive Board may wish to: (a) take note of the present report; (b) express its support for the audit and investigation function assumed by the Office of Audit and Investigations and for strengthening the capacity of the UN-Women Audit Unit; and (c) decide that the Director of Internal Audit will make publicly available all internal audit reports issued after 1 December 2012 with appropriate safeguards for particularly sensitive information.

* UNW/2012/L.4.

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I. Introduction

1. The Office of Audit and Investigations of the United Nations Development Programme (UNDP) submits to the Executive Board of the United Nations Entity for Gender Equality and the Empowerment of Women (UN-Women) its report on internal audit and investigation activities during the period 1 July 2010 to 31 December 2011.

2. The report describes the internal audit and investigation function and its activities, as well as the main audit results that provide insight into the utilization and management of UN-Women resources. It is also forward-looking regarding the services to be provided and the resource requirements for such services.

II. Internal audit function in UN-Women

3. On the basis of financial rule 2302 of the Financial Regulations and Rules of UN-Women, the Under-Secretary-General/Executive Director of UN-Women entrusted the internal audit and investigation function for UN-Women to the Office of Audit and Investigations. In that regard, UN-Women and the Office of Audit and Investigations signed a service level agreement on 5 December 2011, which envisages the establishment of a dedicated UN-Women Audit Unit within the Office and stipulates the objectives and scope of the services to be provided and the funding arrangements.

4. Since the inception of UN-Women on 1 July 2010 and during the transitional period until 31 December 2011, internal audit and investigation services were provided on the basis of the 2008 service level agreement with the predecessor entity, United Nations Development Fund for Women (UNIFEM), and an interim agreement signed with UN-Women in early 2011.

5. The Office of Audit and Investigations conducts its audits in accordance with the International Standards for the Professional Practice of Internal Auditing and the Code of Ethics established by the Institute of Internal Auditors (IIA), which have been adopted by the Representatives of Internal Audit Services of the United Nations Organizations and Multilateral Financial Institutions.

6. The Office of Audit and Investigations is operationally independent of the management of UN-Women and is free to determine the scope of its audits and investigations in accordance with international standards. Moreover, the operations of the Office are governed by a charter, which sets out its purpose, policies and procedures. In that regard, the activities of the Office of Audit and Investigations are subjected to a quality assurance and improvement programme in accordance with IIA Standards. A recent external quality assurance review, conducted in August 2012, has confirmed the general conformity of the Office with the IIA Standards and the Code of Ethics.

7. On the basis of the service level agreement signed in December 2011, the Office of Audit and Investigations established, in January 2012, a dedicated UN-Women Audit Unit, which provides the internal audit services for UN-Women. The staffing of the Unit initially comprised a Chief and an Audit Specialist, both of whom commenced duties in March 2012.

8. Furthermore, in 2012, UN-Women established an Audit Advisory Committee to provide the Executive Director with independent external advice on good practices regarding the organization's accountability framework and systems, including risk management. The Committee will review and comment on the work of the UN-Women Audit Unit, including the audit strategy, annual workplan and budget, periodic progress reports and the annual report to the Executive Board.

9. In order to avoid overlap and to achieve the best use of limited audit resources, the Office of Audit and Investigations coordinates its work with the United Nations Board of Auditors. In that regard, regular consultations have taken place with the previous external auditor, the Auditor General of South Africa. Such interaction now continues with the audit team of the United Republic of Tanzania National Audit Office, which assumed the external audit function for UN-Women on 1 July 2012.

III. Risk-based audit planning

10. In accordance with IIA standard 2010, the Office of Audit and Investigations uses a risk-based audit planning system to ensure that its priorities are consistent with the goals of UN-Women. Risk-based audit planning takes place in two categories, first, for UN-Women field-based activities and secondly, for corporate and headquarters functions and activities.

11. For field offices, the Office of Audit and Investigations uses a risk assessment model, which contains a number of quantitative and qualitative factors that are representative of different types of risks. The model, which covers the UN-Women subregional offices as well as large country programme offices, has been recently revised and updated. It will be revisited and further revised as the Entity's regional architecture evolves.

12. For 2012, the audit work comprises three field-based audits (Afghanistan, Kenya and India). In addition, the Office of Audit and Investigations has conducted a corporate audit risk assessment to determine and better understand the audit universe, identify business and audit risks and determine audit priorities for the short and medium term.

IV. Audits conducted during the transitional period

13. During the transitional period, since the inception of UN-Women on 1 July 2010 until 31 December 2011, the Office of Audit and Investigations provided internal audit and investigation services as a transitional arrangement, which constituted an extension of the services previously provided to UNIFEM and focused on former UNIFEM offices.

14. The following internal audit reports were issued during the transitional period:

(a) UNIFEM Pacific Subregional Office (report No. 719), issued in September 2010: the audit rating was "unsatisfactory", which means that internal controls, governance and risk management processes were either not established or not functioning well. The audit made 23 recommendations, of which 13 were ranked as high priority. Issues raised included a lack of adequate supervision and controls at the management level, poor allocation and monitoring of project budgets,

inadequate supporting documents for payments and non-compliance with procurement procedures through the splitting of contracts to avoid review by the procurement oversight committee. As the United Nations Board of Auditors audited the Pacific Subregional Office in January/February 2012, the Office of Audit and Investigations did not conduct another audit mission, but conducted its follow-up as a desk review;

(b) UNIFEM Arab States Subregional Office (report No. 743), issued in December 2010: the audit rating was "satisfactory", which means that internal controls, governance and risk management processes were adequately established and functioning well. The audit made nine recommendations, of which one was ranked high priority. That recommendation required management to establish a mechanism to track the cumulative values of procurement to ensure that contracts in excess of the threshold are submitted to the procurement oversight committees for review;

(c) UNIFEM Subregional Office for Southern Africa and Indian Ocean Islands (report No. 753), issued in December 2010: the audit rating was "partially satisfactory", which means that internal controls, governance and risk management processes were generally established and functioning, but needed improvement. The audit made 19 recommendations, of which 9 were ranked high priority. The high-priority recommendations aimed at addressing weaknesses in the subregional strategy, staffing structure, procurement reviews, asset management, support services and document management system;

(d) UNIFEM Subregional Office for Mexico, Central America, Cuba and the Dominican Republic (report No. 774), issued in December 2010: the audit rating was "partially satisfactory". The audit made 16 recommendations, of which 8 were ranked high priority. Issues raised included weaknesses in the staffing structure, the absence of a resource-mobilization strategy, inadequate supporting documents, the splitting of contracts, the inappropriate use of contract modalities and deficiencies in the management of assets;

(e) Follow-up audit of UN-Women Southern Cone Subregional Office (report No. 823), issued in May 2011: the follow-up audit was conducted as a result of the overall "unsatisfactory" audit rating that the Office had received during the previous audit, in October 2009 (report No. 688). The on-site follow-up audit showed that the Office had made good progress in addressing the deficiencies identified in the 2009 audit. Of the 24 audit recommendations made, 14 had been fully implemented, while 7 were still in progress. Five of those seven recommendations required action at the corporate level. Three audit recommendations were withdrawn, as they were no longer relevant;

(f) UN-Women Caribbean Subregional Office (report No. 827), issued in October 2011: the audit rating was "partially satisfactory". The audit made seven recommendations, one of which was ranked high priority. The recommendation aimed at addressing weaknesses in the subregional strategy, which did not have baseline data and measurable targets;

(g) UN-Women Subregional Office for Central and Eastern Europe (report No. 863), issued in December 2011: The audit rating was "satisfactory". The audit made nine recommendations, all of which were ranked medium priority.

V. Follow-up on audit recommendations

15. The Office of Audit and Investigations monitors and reports on the implementation status of internal audit recommendations. For this purpose, the Office maintains a web-based database, known as the Comprehensive Audit and Recommendations Database System, to which all audited UN-Women business units have access.

16. The audited units are required to continuously update the status of implementation of audit recommendations in system, starting within one month after the issuance of the audit report and to upload supporting documentation showing the implementation action taken. Based on the updates provided, the Office of Audit and Investigations validates the information received and determines the implementation status.

17. The table below shows the overall implementation rate of audit recommendations as at 31 August 2012, as validated by the Office of Audit and Investigations. Since the establishment of UN-Women in July 2010, the Office has issued seven audit reports containing 107 recommendations. Five of those audits were conducted during the transitional period, while two had been conducted prior to the creation of UN-Women. The table shows that 56 per cent of the recommendations had been implemented by UN-Women, while 29 per cent were still in progress. No implementation action had been taken on 11 per cent of the recommendations, most of which related to corporate policies and procedures. There are 14 high priority recommendations included in the total recommendations still outstanding. Moreover, 25 per cent of the recommendations not yet implemented have exceeded the 18-month mark, and are therefore considered as long outstanding. UN-Women will need to intensify efforts to implement outstanding audit recommendations. The Office of Audit and Investigations is confident that the establishment of an audit focal point and the adoption of additional corporate policies and procedures will lead to significant progress in that regard.

Status of implementation of audit recommendations issued from July 2010 to December 2011, as at 31 August 2012

			Number of recommendations					
Report issued	*Audit ID*	*Audit title*	*Total issued*	*Implemented*	*In progress*	*Not implemented*	*Withdrawn*	*Long-outstanding, high-priority*
September 2010	719	Pacific Subregional Office	23	19	–	3	1	2
December 2010	743	Arab States Subregional Office	9	2	3	4	–	–
December 2010	753	Subregional Office for Southern Africa and Indian Ocean Islands	19	12	6	1	–	2
December 2010	774	Subregional Office for Mexico, Central America, Cuba and the Dominican Republic	16	6	8	2	–	6
May 2011	823	Southern Cone Subregional Office	24	14	7	–	3	4

Report issued	Audit ID	Audit title	Number of recommendations: Total issued	Implemented	In progress	Not implemented	Withdrawn	Long-outstanding, high-priority
October 2011	827	Caribbean Subregional Office	7	4	3		–	–
December 2011	863	Subregional Office for Central and Eastern Europe	9	3	4	2	–	–
July 2010 to December 2011		**Total**	**107**	**60**	**31**	**12**	**4**	**14**
July 2010 to December 2011		**Total (percentage)**	**100**	**56**	**29**	**11**	**4**	**13**

VI. Disclosure of internal audit reports

18. Pending the adoption of a UN-Women policy on the disclosure of internal audit reports, the Office of Audit and Investigations, after consultation with UN-Women, followed, as a transitional arrangement, the disclosure policy applicable to the predecessor entity, UNIFEM. On that basis, the Office disclosed three internal audit reports (on the subregional offices for the Southern Cone; the Caribbean; and Central and Eastern Europe) to the Government of the United States of America. In accordance with the disclosure policy adopted by the Executive Board of UNDP, which was also applicable to UNIFEM, the reports were disclosed on site at the Office of Audit and Investigations and under condition of confidentiality.

19. Meanwhile, the Executive Board of the United Nations Children's Fund (decision 2012/13) and the Executive Board of the United Nations Development Programme, the United Nations Population Fund and the United Nations Office for Project Services (decision 2012/18) have decided that all internal audit reports issued after 1 October 2012 or 1 December 2012, respectively, shall be made publicly available.

20. UN-Women, as a new entity, is committed to organizational transparency and suggests aligning its own disclosure policy and practices to those of the United Nations funds and programmes. This would also foster consistency and coherence within the United Nations system.

21. The Office of Audit and Investigations will exercise proper due diligence prior to making internal audit reports publicly available to ensure the integrity and quality of the information disclosed and to maintain the confidentiality of any information deemed particularly sensitive. Also, prior to public disclosure, the Government concerned, if any, will be given adequate time to comment on the report, thus allowing the Government to bring any confidentiality concerns to the attention of the Director of Internal Audit. If an internal audit report contains information that is deemed to be particularly sensitive (relating, inter alia, to third parties or to a country, Government or administration) or that could compromise pending action or endanger the safety and security of any individual, violate his or her rights or invade his or her privacy, the report may be redacted, or, exceptionally, withheld in its entirety, at the discretion of the Director of Internal Audit.

22. If the Executive Board approves the proposed public disclosure, the Office of Audit and Investigations will post all internal audit reports issued after 1 December 2012 on the UN-Women website. There will be no retroactive disclosure.

VII. Advisory services

23. the Office of Audit and Investigations provided, upon request, advice to UN-Women managers at Headquarters and subregional offices on a range of topics, including the interpretation of regulations and rules, and a review of policies and documents such as the Internal Control Framework, terms of references and grant agreements.

VIII. Investigations

24. In accordance with the service level agreement, the Office of Audit and Investigations provides investigation services, on a cost-reimbursement basis, covering allegations of fraud, corruption or other wrongdoing, including workplace harassment, abuse of authority or retaliation against whistle-blowers, by UN-Women staff members, non-staff personnel and contractors. As such, the Office is the principal channel to receive allegations. To facilitate the reporting of wrongdoing, the Office has established a dedicated UN-Women fraud hotline, which will be accessible through the UN-Women website. The Office has designated one of its investigation specialists as the focal person for all matters relating to UN-Women investigations.

25. Investigations carried out by the Office of Audit and Investigations conform to the principles contained in the Uniform Guidelines for Investigations, adopted by the fourth Conference of International Investigators. The Office conducts fact-finding investigations in accordance with the UNDP Legal Framework for Addressing Non-Compliance with United Nations Standards of Conduct and as further elaborated in the Investigations Guidelines of the Office.

26. To date, the Office of Audit and Investigations has received two complaints alleging wrongdoing by UN-Women staff members. The allegations of one case were not substantiated and the case was closed after initial assessment. Investigations are continuing on the second case, which was received in July 2012. The Office expects that, with the activation of the fraud hotline, the number of complaints will increase.

IX. Staffing and budget

27. Total expenditures for UN-Women internal audit activities in 2011 were approximately $200,000. For 2012, UN-Women and the Office of Audit and Investigations envisage an increased level of services, resulting in an approved budget of $438,186. The 2012 budget comprises salary costs of $351,468 and general operating expenditures, in particular travel cost, of $86,718.

28. During the transitional period, the Office of Audit and Investigations provided the services of one Audit Specialist in 2011. The staff member retired in October 2011 and the post remained vacant until the end of the year. The December 2011

service level agreement provides for two staff members — a Chief at the P-5 level and an Audit Specialist at the P-3 level. This is equivalent to 400 working days per year for audit activities, audit management and advisory activities. The 2012 audit workplan has been prepared within the framework of these available resources.

29. The current resource level provides for the minimum capacity necessary for UN-Women internal audits. The recently conducted audit risk assessments, the increase in UN-Women resources and activities and the broad field presence resulting from the envisaged future regional architecture have given rise to a need to revisit and reassess the resource requirements for audit. In that regard, the Office of Audit and Investigations has been guided by the suggested benchmarks for the resourcing of internal audit functions, established by the Joint Inspection Unit of the United Nations system in its report entitled "Oversight lacunae in the United Nations system" (A/60/860) and reconfirmed in its report entitled "The audit function in the United Nations system" (A/66/73). The Joint Inspection Unit proposes one auditor position for an annual expenditure volume of $60 million to $100 million, taking into account whether it is a headquarters- or field-based organization. UN-Women expenditures in 2011 totalled close to $200 million. Even without the expected further budget increase for UN-Women, the current resource level for audit provides for a minimum capacity. Such capacity might be sufficient for a headquarters-based organization. With the broad and further expanding presence of UN-Women in the field, however, the current resource level is inadequate and falls below minimum standards. The Office of Audit and Investigations will discuss future resource requirements with UN-Women senior management in order to bring the capacity of the UN-Women internal audit function in line with the recommended benchmarks for the United Nations system and to enable the internal audit function to provide reasonable assurance on the use of UN-Women resources.